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STATE OF INDIANA

INDIANA UTILITY

INDIANA UTILITY REGULATORY COMMISSION REGULATORY COMMISSION

PETITION OF SOUTHERN INDIANA GAS AND) D/B/A **VECTREN**) ELECTRIC **COMPANY** ENERGY DELIVERY OF INDIANA. ('VECTREN SOUTH-GAS") FOR (1) AUTHORITY TO INCREASE ITS RATES AND CHARGES FOR GAS UTILITY SERVICE; (2) APPROVAL OF NEW RATES AND **CHARGES** SCHEDULES OF APPLICABLE THERETO; (3) AUTHORITY, TO THE **EXTENT NECESSARY** AS PLAN. **ALTERNATIVE** REGULATORY TO RECOVER ITS UNACCOUNTED FOR GAS COSTS AND THE GAS COST COMPONENT OF ITS BAD DEBT EXPENSE IN ITS GAS COST ADJUSTMENT FILINGS; (4) APPROVAL OF A DISTRIBUTION REPLACEMENT ADJUSTMENT TO RECOVER THE COSTS OF A PROGRAM FOR THE ACCELERATED REPLACEMENT OF CAST IRON MAINS AND BARE STEEL MAINS AND SERVICE LINES; (5) APPROVAL OF THE **IMPLEMENTATION OF** THE SALES RECONCILIATION COMPONENT OF THE ENERGY EFFICIENCY RIDER PROPOSED IN CAUSE NOS. 42943 AND 43046 OR OTHER RATE DESIGN CHANGES THAT UNLINK ITS FIXED COST RECOVERY FROM ITS SALES VOLUME; APPROVAL AS AN**ALTERNATIVE** REGULATORY PLAN PURSUANT TO IND. CODE § 8-1-2.5-6 OF A RETURN ON EQUITY TEST TO BE USED IN LIEU OF THE STATUTORY NET OPERATING INCOME TEST IN ITS GAS COST ADJUSTMENT PROCEEDINGS: (7) AUTHORITY PURSUANT TO 170 IAC 5-1-27(F) FOR A NON-GAS COST REVENUE TEST TO DETERMINE REQUIRED WHEN DEPOSITS ARE FACILITIES EXTENSIONS; AND (8) APPROVAL OF VARIOUS CHANGES TO ITS TARIFF FOR GAS SERVICE, INCLUDING INCREASES IN CERTAIN NON-RECURRING CHARGES.

CAUSE NO. 43112

CERTIFICATE OF SERVICE

This is to certify that a copy of the foregoing OUCC TESTIMONY AND EXHIBITS has been served upon the following parties of record in the captioned proceeding by electronic service and/or by depositing a copy of same in the United States mail, first class postage prepaid, on March 16, 2007.

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SUPPLEMENTAL DIRECT TESTIMONY

OF

TYLER E. BOLINGER

INDIANA OFFICE OF UTILITY CONSUMER COUNSELOR

PUBLIC'S EXHIBIT NO. S-1

MARCH 2007

Cause No. 43112 Vectren South - Gas Supplemental Testimony of Tyler E. Bolinger

Introduction

1	Q:	Please state your name and business address.
2	A:	My name is Tyler E. Bolinger, and my business address is Indiana Government Center
3		North, Room N501, Indianapolis, Indiana 46204.
4	Q:	By whom and in what capacity are you employed?
5	A:	I am employed by the Indiana Office of Utility Consumer Counselor (OUCC) as the
6		Director of Natural Gas.
7	Q:	Have you previously filed direct testimony in this Cause?
8	A:	Yes. On February 27, 2007, I filed direct testimony regarding Vectren South's bare steel
9		and cast iron replacement program (Program) and the proposed Distribution Replacement
10		Adjustment (DRA) tracker mechanism. My credentials are described in that testimony.
11		(Pub. Exh. No. 5)
12	Q:	What is the purpose of your supplemental testimony?
13	A:	I will review and support the Settlement Agreement (Settlement) in this Cause between
14		Vectren South, the OUCC, and A.K. Steel.
15	Q:	Please briefly describe your knowledge of this rate case and the Settlement.
16	A:	I am familiar with all aspects of the case and the Settlement, including revenue
17		requirements, cost of service and rate design, and policy issues such as Vectren South's
18		proposals to modify the ratemaking treatment of bad debt expense and unaccounted for

gas costs.	I have	worked	extensively	throughout	these	proceedings	with	all	of	the
OUCC's te	chnical a	and legal	experts and	with the Par	ties in	settlement ne	egotia	tion	s.	

Please briefly describe the Settlement.

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The Settlement resolves all issues in this Cause. The Settlement describes in detail the various pro forma adjustments to test year revenues and expenses. With regard to pro forma adjustments, Appendix C of the Settlement depicts Vectren South's and the OUCC's positions in their respective cases-in-chief, Vectren South's rebuttal positions, and the final compromise agreement of the Parties on pro forma adjustments. The Settlement, including the appendixes, provides detailed explanations of the various pro forma adjustments and the proposed resolution of related issues by the Parties. The agreement of the Parties on pro forma adjustments is also well supported by case-in-chief and rebuttal evidence already filed by the Parties in this case.

The Settlement provides for new base rates designed to produce additional utility operating revenue of \$5,334,907. The Parties have agreed to an "across the board" allocation of the revenue increase, which simply means that each rate class will see approximately the same percentage increase in their rates and charges. Rates for residential sales service have been determined by increasing the monthly customer facilities charge from \$10.75 to \$11.00 and allocating the remaining revenue increase to the block rates on an equal per therm basis.

The Settlement also resolves several policy issues, including a continuation of Vectren South's Pipeline Safety Adjustment (PSA) mechanism, Vectren South's bare steel and cast iron replacement program and the related Distribution Replacement Adjustment (DRA) mechanism. The Settlement also provides new approaches to the

1		ratemaking treatment of unaccounted for gas (UAFG) and bad debt expense. Below I
2		will elaborate on these policy issues and the reasonableness of the compromises reached
3		by the Parties.
4	Q:	Is the Settlement the result of good faith negotiations among the Parties?
5	A:	Yes, it certainly is. The bulk of the negotiations took place after the Parties had all pre-
6		filed their cases-in-chief. Thus the issues had been extensively researched by the Parties
7		who were well informed about the issues and about the costs and risks associated with the
8 ·		litigation alternative. This set the stage for constructive, good faith negotiations,
9		reasonable compromises, and overall resolution of the case.
10	Pipeli	ne Safety Adjustment (PSA)
11 12 13	Q:	Does Vectren South currently have a Pipeline Safety Adjustment (PSA) mechanism designed to provide rate recovery for incremental expenses caused by the requirements of the Pipeline Safety Improvement Act of 2002 (Act)?
14	A:	Yes. This mechanism was initially established in Cause No. 42596, Vectren South's last
15		rate case. Under the terms of the settlement in that Cause, a detailed review of the PSA
16		was scheduled to take place in the spring of 2007. During the pendency of the current
17		rate case, the OUCC and Vectren South had extensive discussions concerning the PSA.
18		Both Vectren South and the OUCC believed that we had adequate information to conduct

Vectren South desired a continuation of the PSA. Through OUCC witness Grosskopf's testimony the OUCC agreed in principle that the PSA should be extended (Pub. Exh. 2.). The OUCC agrees with Vectren South that the costs of complying with the Act remain highly uncertain. Therefore, the OUCC supports an extension of the PSA.

the scheduled spring 2007 PSA review as part of our work on the current rate case.

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On rebuttal, Vectren South witness Albertson provided more details about the terms on which the PSA should be extended. (Pet. Exh. SEA-1R) He also informed the Commission of the intention of Vectren South and the OUCC to reach final agreement on terms for an extension of the PSA. Shortly after the rebuttal filing, Vectren South and the OUCC finalized their agreement on an extension of the PSA, and that agreement is contained in the Settlement.

Section 6 of the Settlement describes in detail the terms on which the Parties have agreed to extend the PSA through the annual PSA filing for the twelve months ended March 31, 2010. At that time, the Parties will review the PSA to consider the appropriateness of the annual cap, whether the PSA should continue, whether expenses have levelized sufficiently to be included in base rates, and any other related matters. A great deal of thought, discussion and effort has gone into the new agreement to extend the PSA. The new agreement on the PSA is very reasonable in light of the on-going challenges and uncertainty surrounding compliance with the Act

GCA Ratemaking Treatment of Unaccounted For Gas Costs

Q: Did Vectren South propose a change in the ratemaking treatment for the costs of unaccounted for gas (UAFG)?

Yes, Vectren South proposed dollar-for-dollar tracking of UAFG costs along with other gas costs in the GCA. Traditionally, and in sharp contrast to other gas costs, an allowance for unaccounted for gas has been embedded into base distribution rates for GCA sales customers and not tracked for ratemaking purposes. This traditional approach provides arguably the maximum incentive for gas utilities to manage and minimize unaccounted for gas.

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Utilities like Vectren South express concern with the traditional approach primarily because it provides no relief for market changes in the price of commodity gas. For example, if a utility's embedded base rate provision for UAFG was determined when commodity prices were at \$3.00 per Dth, then the utility would be disadvantaged if commodity prices rise to \$6.00 for reasons outside management's control. This would be true even if the utility had carefully managed its UAFG ratio or even driven it down slightly.

The intention of the traditional approach is to provide strong incentives to manage UAFG. The OUCC strongly supports that goal, but we are cognizant of high and volatile commodity prices, over which management has very limited control. The OUCC expressed willingness to compromise on this issue if incentives to manage the UAFG ratio can be maintained. For GCA ratemaking purposes, the Settlement provides for a cap on the UAFG ratio of 1.2%. Up to that cap, Vectren South may recover in the GCA the actual UAFG costs associated with volumes provided to GCA sales customers. If the UAFG ratio rises above 1.2%, then recoverable UAFG costs in the GCA will be calculated based on the 1.2% ratio, and no recovery would be provided for unaccounted for volumes above the 1.2% level. This compromise maintains a clear incentive for Vectren South to diligently manage its UAFG ratio, while also being responsive to Vectren South's concern about its lack of control over volatile commodity prices. This is a reasonable compromise for Vectren South and its GCA customers and should be approved by the Commission.

Ratemaking Treatment of Bad Debt Expense

Q: What is the traditional ratemaking treatment of bad debt expense?

An amount for bad debt (i.e. net write-offs of accounts receivable) has traditionally been
embedded into base rates for Indiana gas utilities, with no tracking between rate cases.
The amount is typically calculated by applying a reasonable bad debt ratio (a percentage)
to pro forma utility operating revenue to obtain pro forma bad debt expense. In this case,
the OUCC proposed a bad debt ratio of 0.60%, and Vectren proposed a 0.70% ratio in
rebuttal. This is not an extremely large difference and both proposals were based on
recent actual experience. In settlement, the Parties have agreed to use a 0.65% bad debt
ratio for ratemaking purposes.

What changes did Vectren South propose to the ratemaking treatment of bad debt?

Vectren South proposed to split bad debt into two primary components: (1) the gas cost component; and (2) the margin (i.e. non-gas cost) component. This latter (margin) component is associated with the provision of distribution service to GCA sales customers and transportation service to larger customers. The former (gas cost) component is associated with the provision of gas supply to GCA sales customers.

In my opinion, this split of bad debt into two primary components is logical and sound. It also permits consideration of alternative ratemaking approaches that reflect the fundamental differences between distribution/transportation service and utility gas supply service to GCA customers.

How did Vectren South propose to treat these two (2) components of bad debt?

Vectren South proposed to embed an amount into base rates to provide for the margin component of bad debt, with no tracking. Vectren South proposed that it begin recovering the gas cost component of bad debt in the GCA on a dollar-for-dollar basis. Through Mr. Galligan's testimony, the OUCC expressed concern about a possible

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weakening of incentives to manage bad debt caused by dollar-for-dollar tracking of the gas cost component of bad debt, which is by far the larger of the two components. Again through Mr. Galligan's testimony, the OUCC suggested an alternative based on a fixed bad debt ratio applied to total gas costs in the GCA. Under this approach, Vectren South's opportunity to recover the gas cost component of bad debt would rise and fall with the price of gas but would always be calculated based on the fixed bad debt ratio determined at the time of the base rate case. When compared to dollar-for-dollar tracking, the OUCC believes this approach provides stronger incentives for the utility to maintain or even drive down its bad debt ratio. ¹

Q: How did the Parties resolve bad debt for ratemaking purposes?

- A: First, the Parties agreed to a 0.65% bad debt ratio, which is well supported by recent historical experience. Second, the Parties agree that it is reasonable to split bad debt into two components (gas cost and margin). The Parties also agree that different approaches should be used to recover the gas cost and margin components of bad debt.
- What agreement did the Parties reach regarding the margin component of bad debt?
- 17 A: The margin component of bad debt will be embedded into base rates, with no tracking whatsoever. The amount embedded reflects the agreed 0.65% bad debt ratio.
- 19 Q: What agreement did the Parties reach regarding the gas cost component of bad debt?
- 21 A: The Parties have agreed to the alternative approach proposed by the OUCC, and this is 22 described in Section 5 of the Settlement. No amount will be embedded into base rates for 23 recovery of the gas cost component of bad debt. In each GCA, the fixed bad debt ratio of

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See Mr. Galligan's testimony in this Cause (Pub. Exh. No. 4.) The OUCC made a similar proposal on bad debt through OUCC witness Bolinger's testimony in the recent Citizens Gas rate case (Cause No. 42767). However, no agreement on the issue was reached in that case.

.65% will be applied to total gas costs to determine "recoverable bad debt gas costs." As used in the Settlement, the term "bad debt gas cost" is synonymous with the term "gas cost component of bad debt" that I have described above.

This new methodology provides an improved opportunity for the utility to fully recover its gas costs by recognizing that some accounts will be written off as uncollectible. Also, the accuracy of recovery should improve because the opportunity for recovery will move up and down with the price of gas, a variable over which management has very limited control. Finally, strong incentives to manage bad debt and the bad debt ratio will be maintained by using a fixed bad debt ratio of .65%. Management has much more control over the bad debt ratio than it has over the price of gas. If management can reduce the bad debt ratio between rate cases, then the Utility stands to gain. The reverse is also true. The OUCC supports this incentive and this new approach to the gas cost component of bad debt.

Bare Steel and Cast Iron Replacement Program

- Q: Were there disagreements in this case regarding the proposed bare steel and cast iron replacement program (Program) described by Vectren South's witness Mr. Francis (Pet. Exh. JMF-1)?
- 18 A: The Program itself generated little, if any, controversy. However, the proposed
 19 Distribution Replacement Adjustment (DRA) mechanism was a source of disagreement.
 20 My own direct testimony explained OUCC objections to the DRA, which I described as a
 21 capital cost tracker. I also described a possible alternative that would permit so called
 22 "post-in-service AFUDC and deferred depreciation expense" on projects that are part of
 23 the Program.

The OUCC strongly supports the eventual replacement of bare steel and cast iron from Vectren South's system, but we are not convinced that a capital cost tracker, like the DRA, is appropriate.

How did the Parties resolve these issues in settlement?

The Settlement provides for "post-in-service AFUDC and deferred depreciation expense" on projects that are part of the Program. As described in Section 7 of the Settlement, investments made pursuant to the Program will be accounted for as separate projects, following current project accounting practices at Vectren South. The amount of investments made that are eligible for post-in-service AFUDC and deferred depreciation treatment (Accounting Treatment) will be limited to \$3.0 Million per year. The Accounting Treatment is generally limited to a three year period beyond the in service date of the project. This provision will help to ensure that extremely large deferrals do not accumulate over time. The three (3) year limitation may result in more frequent base rate reviews than would be the case with no limitation on deferrals. However, periodic base rate reviews every few years are generally to be expected for utilities with large construction programs.

The OUCC supports the Accounting Treatment related to the Program described in Section 7 of the Settlement. This is a reasonable compromise that is responsive to Vectren South's concerns about earnings attrition and the OUCC's concerns capital cost trackers in the gas utility industry, as described in my direct testimony.

Conclusion

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Q: Do you recommend Commission approval of the Settlement?

Yes. The Settlement represents a compromise among the Parties on many	/ disputed
issues. This compromise was reached through good faith bargaining an	nong well
informed Parties. The Settlement, including the appendixes, describ	bes these
compromises in detail. The additional testimony filed in support of the	Settlement
provides additional explanations and support for the Settlement. The evidence	of record
also contains extensive evidence regarding all issues in this Cause, because the	Parties all
filed their cases-in-chief, and Vectren filed its rebuttal testimony.	

I recommend that the Commission approve the Settlement between Vectren South, the OUCC, and A.K. Steel in this Cause.

- 10 Q: Does this conclude your testimony?
- 11 A: Yes.

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